BUYING OR SELLING SALONS

HERE'S HOW YOU LEARN THE LINGO! By Nikki Katz

Reading an advertisement for a salon for sale can be a very confusing exercise. We have put together a list of all the common phrases and abbreviations, so you know what you are looking at. Although these terms can be interpreted differently across other industries, this is what they usually mean in the salon & spa business.

1. Total Sales/Turnover/Revenue: This is the total amount of sales generated in a business and is an indicator of how big the business is. For example, if a salon has 1 staff member the total sales for the year would be their service sales + retail sales + any other income generated like gift vouchers. The bigger the turnover often means the bigger the profit you can get out of the business. Eg – 1 staff member did $2000 in services for the week + $300 in retail = $2300 x 52 weeks = $120,000 Total Sales approximately.

2. Cost of Goods (COGS): this is what it costs to do the service, in industry it most commonly is the actual product used. A benchmark for cost of goods vs total sales is usually around 7-12% in hairdressing and a little higher in beauty. A good business will have a low cost of goods percentage. To work out a cost of goods percentage; all you need to do is take the total cost of product used in the business and divide by the total sales of the business then multiply by 100. Eg - $10,000 product ÷ $120,000 total sales x 100 = 8.3%.

3. Gross Profit (GP)/Gross Margin (GM): this figure is a bit boring within our industry and all it relates to is the Total Sales minus the Cost Of Goods. Gross Profit varies from hair to beauty. In a barber shop where there is limited product used the GP would be very high at around 98%, in a ladies salon the GP would be around 90% and in a beauty salon the GP would come in at around 85% due to these salons using expensive products within their treatments.

4. Wage percentage: one of the most important figures you will see in business is the amount of wages spent vs the total sales of the business. In most salon enterprises it is difficult to get this down below 40% of total sales however it is a good indication of where you can improve the business. The lower the wage percentage the better. To work this out all you need to do is take the total wages figure including superannuation and divide by the total sales then multiply by 100. Eg - $45,000 wages ÷ $120,000 total sales x 100 = 37.5%.

5. Rent per square meter (sqm): a key area in any business is rent vs the location of the business. It is essential to have a good location but make sure you are not paying too much for it. The easiest way to benchmark rent is to break it down into a dollar value per square meter. For example a salon in Sydney CBD Westfield Shopping Centre would come in at around $2700 per sqm. Some might say that's expensive but that rent guarantees millions of people each year walking past your door. Most shopping centre rents are in the vicinity of $1500 per sqm. Strip Shops around $1000 per sqm and boutique (not on main road) sites can be as cheap $150 per sqm. Cheap rent and good location is the key but this is never easy to find.

6. Stock at Value (SAV): this is often tacked on to the price of a business and suggests that you will be required to purchase the salon at a certain price plus you will be required to purchase the current stock in the business as well. In most sales the stock value is capped at a certain level and when it comes to the stocktake at settlement most of the open stock items are not counted in this figure. Eg – Sale Price - $100K (By the way K means thousand) + SAV

7. Walk In Walk Out (WIWO): the other option when buying a business is to purchase it on a WIWO basis where all the stock is included in the sale price. This often happens if the business does not have a lot of stock (less than $5000) or the owner just wants to sweeten the deal. Eg Sale Price - $100K WIWO.

8. Net Profit: once you have paid all your bills then hopefully at the end is a net profit. This is by far the most important figure when buying or selling a salon. Often the net profit may be small at around $15-$20K however the owner lives an extravagant lifestyle … trips to Paris each year, leases a Porsche, home office etc. This is done to lower the net profit and avoid paying too much tax. By the way all this can be done quite legally. When selling a salon, many of these expenses can be 'added back' into the net profit as the new owner may be a bit more restrained with their expenses. Always remember the bigger the net profit the higher the sale price will be on a salon.

9. Earnings Before Income Tax (EBIT): this very important term relates to net profit and how it is displayed. An EBIT net profit means that the owner has taken a wage and there is still profit at the end of the day. This is often referenced to managed salons where the owner does not work in them. An EBIT profit is one the cleanest profit figures you can get and this type of profit commands the best sales price of a salon. That's why managed salons are always in hot demand.

10. Proprietors Earnings Before Income Tax (PEBIT): this type of profit has the owners wage added back into the net profit which means it is not as appealing as an EBIT profit. You don't need to get too hooked up on this concept, just understand that both are a way of representing net profit.

11. Addbacks: when calculating the real net profit of a business it is a common practice to add back into the net profit certain expenses to give a true indication of the actual money you will earn out of the business. Justifiable addbacks are depreciation, one off expenses like getting sued, interest on a loan, often business coaches, leasing of motor vehicles, overseas trips, excess wages or superannuation. All of these expenses can be stopped when you buy the business so they are justifiable addbacks and therefore money in your pocket.

12. Return on Investment (ROI): this figure is very important as it lets you know how quickly you will get your money back on your investment. For example if a salon had an EBIT net profit of $100K and you purchased the salon for $200K then your ROI would be 50% which means you would make you money back in 2 years. That would be pretty good. In most cases the higher the ROI the better the investment. To work out ROI all you need to do is take the net profit and divide it by the sale price of the business then multiply by 100. EG $100K ÷ $200K x 100 = 50%.

13. Now that you understand the basics of buying and selling all you need to do hunt around for a good deal and jump on it quickly. If you're selling; now you know what you need to do to make your business attractive to a potential buyer. Goodluck.

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